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No. 126

Supreme Court of the United States

OCTOBER TERM, 1960.

LAURENS FEDERAL SAVINGS AND LOAN ASSOCIATION, Petitioner

versus

SOUTH CAROLINA TAX COMMISSION, and OTIS W. LIVINGSTON, Chairman et al., Respondents

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF SOUTH CAROLINA

BRIEF FOR RESPONDENTS

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INDEX

	PAGE
Opinions Below	1
Jurisdiction	1
Counter Statement of Question Presented for Review	2
Statutes Involved	2
Statement	2
Summary of Argument	4
Argument:	
I. The Imposition of South Carolina Documentary Taxes Upon the Creation of Promissory Notes in South Carolina by Petitioner is Authorized does not Infringe Any Act of Congress	5
II. Discussions of Decisions Bearing on the Question	8
Conclusion	12
Appendix	~~13~~ 15
Certificate of Service	21

CITATIONS

Cases: PAGE

Alabama v. King & Boozer, 314 U. S. 1, 9, 62 S. Ct. 43, 140 A. L. R. 15 6

Austin v. Boston, 7 Wall (U. S.) 694, 19 L. Ed. 224 7

Burnet v. Coronado Oil & Gas Co., 285 U. S. 393, 52 S. Ct. 443 6

Carson v. Roane-Anderson Co., 342 U. S. 232 6

Federal Land Bank v. Crosland, 261 U. S. 374, 43 S. Ct. 385 ..... 9, 11

First Federal Savings and Loan Association of Altadena v. Johnson, 49 Cal. App. (2d) 465, 122 P. (2d) 84 10

Graniteville Manufacturing Co. v. Query, 44 F. (2d) 64, Aff., 283 U. S. 376, 51 S. Ct. 515 4

Helvering v. Mountain Producers Corp., 303 U. S. 376, 387, 58 S. Ct. 623 6

James v. Dravo Contracting Co., 302 U. S. 134, 58 S. Ct. 208, 114 A. L. R. 318 7

Lawrence v. Shaw, 300 U. S. 245 6

McCulloch v. Maryland (1819), 4 Wheat (17 U. S.) 316, 46 L. Ed. 579 6

Penn Dairies v. Milk Control Commission, 318 U. S. 261, 63 S. Ct. 617 6

Pittman v. Home Owners' Loan Corporation, 308 U. S. 21 ..... 8, 9, 11

Plymouth Citrus Growers Association v. Lee, Comptroller (1946), 27 So. (2d) 415, 157 Fla. 893 11

Reynolds Metal Co. v. Martin, 107 S. W. (2d) 251, 269 Ky. 378, App. Dismissed, 58 S. Ct. 146, 302 U. S. 646 6

State v. Minnesota Federal Savings and Loan Association, 218 Minn. 220, 15 N. W. (2d) 568 9

Trotter v. Tennessee, 290 U. S. 354 6

CITATIONS—Continued

Statutes: PAGE

Federal Home Loan Bank Act, c. 522, 47 Stat. 725:

12 U. S. C. 1422 15

12 U. S. C. 1424 15

12 U. S. C. 1426(e) 16

12 U. S. C. 1430(a) 17

12 U. S. C. 1430(c) 17

12 U. S. C. 1433 ..... 2, 3, 18

Home Owners' Loan Act of 1933, c. 64, 48 Stat. 128:

12 U. S. C. 1462(d) 19

12 U. S. C. 1464(a) 2, 7, 19

12 U. S. C. 1464(h) 4, 7, 8, 9, 10, 19

12 U. S. C. 1464(k) 20

Federal Farm Loan Act of July 17, 1916, c. 245, Sect. 26, 39 Stat. 360:

12 U. S. C. 931 9

Farm Credit Act of 1933:

Section 68, 12 U. S. C. 1138 11

Code of Laws of South Carolina (1952), Volume 6, Title 65:

Section 65-688 ..... 2, 20

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ON WRIT OF CERTIORARI TO THE SUPREME COURT OF SOUTH CAROLINA

BRIEF FOR RESPONDENTS

OPINIONS BELOW

The opinion of the Supreme Court of the State of South Carolina to which this matter relates (R. 15-23) is officially reported at 236 S. C. 2 and at 122 S. E. (2d) 716.

JURISDICTION

The jurisdiction of this Court is correctly stated in petitioner's brief.

COUNTER STATEMENT OF QUESTION PRESENTED FOR REVIEW

Do the provisions of 12 U. S. C. 1464(h) serve to permit the imposition by respondents of South Carolina documentary stamps on promissory notes made in South Carolina by petitioner to the Federal Home Loan Bank of Greensboro, North Carolina, or, is such taxation precluded by the provisions of 12 U. S. C. 1421 *et seq.*, particularly 12 U. S. C. 1433?

STATUTES INVOLVED

The provisions of the pertinent portions of the statutes for consideration by the Court are set out in the Appendix, *infra*.

STATEMENT

The petitioner is a federally chartered Savings and Loan Association, doing business at Laurens, in the State of South Carolina. As such, it is a member of the Federal Home Loan Bank of Greensboro, North Carolina (R. 16) and was chartered pursuant to the provisions of the Home Owners' Loan Act of 1933 (12 U. S. C. 1464(a)) (R. 3, 7). The "Bank" itself, that is the Federal Home Loan Bank of Greensboro, was created by the Federal Home Loan Bank Act of July 22, 1932 (12 U. S. C. 1421 *et seq.*) and represents the Federal Home Loan Bank System in that geographical area wherein petitioner is located.

Within the State of South Carolina, at Laurens, the petitioner made and executed certain promissory notes to the "Bank" as the Federal Home Loan Bank of Greensboro will be called hereinafter (R. 17).

Section 65-688 of the 1952 South Carolina Code of Laws imposes a documentary stamp tax upon promissory notes geared to the amount of such note, that is, four (4¢) cents for a sum not exceeding One Hundred and no/100

($100.00) Dollars, and for each additional One Hundred and no/100 ($100.00) Dollars or fractional part thereof, four (4¢) cents. (Appendix, *infra.*) Under the provisions of this South Carolina statute, documentary taxes in the sum of Two Thousand Two Hundred Seventy and no/100 ($2,270.00) Dollars, in relation to promissory notes executed by petitioner in South Carolina, were assessed by respondents and paid under protest by petitioner (R. 15). There is no dispute with respect to correctness of the amount of the taxes assessed but rather petitioner sued to recover the entire sum paid under protest, the petitioner conceiving that the taxes were assessed illegally and wrongfully by virtue of Acts of Congress and in direct violation of a tax exemption granted to petitioner and to the "Bank" by the terms of the Federal Home Loan Bank Act, 12 U. S. C. 1421 *et seq.* (R. 6). The trial Court, as well as the Supreme Court of South Carolina (R. 15-23), held that the taxes were authorized by Federal law. An *amicus curiae* brief has been filed by the United States and the interest of the United States has been set forth therein.[1]

The provisions of 12 U. S. C. 1433 of the Federal Home Loan Bank Act prescribe certain exemptions from taxation by the United States and by the States.[2] The provisions of the Home Owners' Loan Act of 1933, under which the petitioner was chartered as a Federal Savings and Loan As-

[1] The interest of the United States is stated in part, "State taxation of promissory notes given for advances to the Federal Savings and Loan Associations by the Federal Home Loan Bank System is in violation of the express exemption provided by Congress and impairs the national policy" (Brief of *Amicus Curiae*, p. 4).

[2] These exemptions include "any and all notes, debentures, bonds, and other such obligations issued by any bank, and consolidated Federal Home Loan Bank bonds and debentures." Additionally, "the bank, including its capital, reserves and surplus, its advances, and its income, shall be exempt from all taxation". c. 522, Section 13, 47 Stat. 735, 12 U.S.C. 1433.

sociation, likewise contain exemptions from taxation.[3] The Supreme Court of South Carolina rendered its opinion holding that the respondents had properly assessed and collected the South Carolina documentary stamp taxes, Congress having granted the taxing authority that right by virtue of 12 U. S. C. 1464(h) (R. 23).

SUMMARY OF ARGUMENT

Has Congress waived immunity from taxation so as to permit the respondents to impose and collect the South Carolina documentary taxes from the petitioner? The taxes were not imposed upon the "Bank" and further the "Bank" was not required to reimburse the petitioner for the taxes paid and thus the economic burden of the tax was not upon the United States. Furthermore, the legal incidence of the tax is on petitioner and not on the Bank. As a matter of fact, this Court has construed the same provisions of the South Carolina law and has held that this tax is an excise tax, of a familiar sort, levied with respect to the creation of instruments within the state.[4] The Court stating:

> "It is simply a tax levied in relation to an act done within the state in making an instrument."

Thus, the promissory notes were the instruments created in South Carolina. Created by whom? By the maker thereof, the petitioner, and upon whom rests or falls the legal incidence of the tax.

It is contended by petitioner that to tax the instrument made and created in South Carolina by it, is to tax the "advances" of the "Bank" which is denied to the respond-

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[3] The pertinent provision reads, "and no State, * * *, shall impose any tax on such associations or their franchise, capital, reserves, surplus, loans, or income greater than that imposed by such authority on similar local mutual or cooperative thrift and home financing institutions." c. 64, Section 5, 48 Stat. 133, 12 U.S.C. 1464(h).

[4] *Graniteville Manufacturing Co. v. Query*, 44 F. (2d) 64, aff. 283 U. S. 376, 51 S. Ct. 515.

ents by virtue of the Act of Congress establishing the Federal Home Loan Bank system. Even petitioner, however, asserts, at most, that the tax is "an indirect impost upon the Bank (*sic*) 'advances' which Congress intended to remain immune from State taxes".[5]

It has not been contended by petitioner that South Carolina has discriminated with respect to it as it has applied the statute similarly with regard to state chartered associations. The South Carolina tax is not imposed upon an "advance" of the "Bank" but rather is imposed upon the instruments created in South Carolina by petitioner, and thus does no violence to the Act of Congress denying to the States the right to tax "advances" of a member Bank of the Federal Home Loan Bank system.

The South Carolina Supreme Court decision herein is proper in holding that the taxes as imposed do not infringe the Act of Congress.

ARGUMENT

I

The imposition of South Carolina documentary taxes upon the creation of promissory notes in South Carolina by Petitioner is authorized and does not infringe any Act of Congress.

No constitutional attack is made in this matter but rather the case is bottomed upon the claim that the South Carolina tax does violence to provisions of Federal legislation which petitioner claims denies to the respondents the right to impose the taxes.[6] Despite this, however, it will serve well to cover certain well established principles which have resulted, in large measure, from decisions wherein constitutional objections were raised.

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[5] Brief of petitioner, page 14.
[6] Brief of petitioner, page 15.

Beginning with the case of *McCulloch v. Maryland* (1819), 4 Wheat (17 U. S.), 316, 46 L. Ed. 579, it has been firmly established that the several states may not tax the United States, its properties or its agencies and instrumentalities created to carry out its lawful functions. Likewise established is the fact that the power to tax is inherent in the states' sovereignty and is essential to its existence and the power may be exercised without limit except to the extent that it may be prohibited by State or Federal Constitutions. *Reynolds Metal Co. v. Martin*, 107 S. W. (2d) 251, 269 Ky. 378, App. dismissed, 58 S. Ct. 146, 302 U. S. 646. It is further well settled that Congress has the power to bring into being an agency to carry out governmental functions and it has the power, under the Constitution, to preserve those functions. *Lawrence v. Shaw*, 300 U. S. 245; *Trotter v. Tennessee*, 290 U. S. 354; *Carson v. Roane-Anderson Co.*, 342 U. S. 232.

Equally fundamental and well established in the law are several other important principles. One of these is that a tax to be objectional must be a **direct and substantial** burden upon the government or upon the exercise of its legitimate functions. Generally, **indirect** or **remote** taxes are not objectionable even though the economic burden of the tax finally rests upon the government. *Helvering v. Mountain Producers Corp.*, 303 U. S. 376, 387, 58 S. Ct. 623; *Burnet v. Coronado Oil & Gas Co.*, 285 U. S. 393, 52 S. Ct. 443; *Penn Dairies v. Milk Control Commission*, 318 U. S. 261, 63 S. Ct. 617; *Alabama v. King & Boozer*, 314 U. S. 1, 9, 62 S. Ct. 43, 140 A. L. R. 15.

In the instant matter, it is respectfully submitted that the tax is upon the creation of an instrument in South Carolina by the petitioner for the exaction of which Congress has waived immunity by the terms of the very act under

which petitioner is created,[7] and is not an exaction of taxes from the "Bank" which is created under a separate and distinct Act of Congress.[8]

The "Bank" and the petitioner are separate and distinct entities, the taxation of which is dealt with in two separate and distinct Acts of Congress. This becomes important when the reasons advanced by petitioner for holding the tax to be invalid are considered. The reasoning urged by petitioner is that Congress has provided that "advances" of the Home Loan Banks are exempt from taxes, that the petitioner, as a savings and loan association, makes its notes to be submitted to the Bank so as to obtain "advances", that thereby the tax is on the "advances" of the "Bank", which to tax is to impair and burden the home financing and thrift program of the United States being carried out through the federal savings and loan associations.

As a matter of fact, Congress may waive either wholly or partially, or with such limitations and qualifications as Congress may deem proper, the exemption of its instrumentalities from state taxation. *Austin v. Boston*, 7 Wall (U. S.) 694, 19 L. Ed. 224; *James v. Dravo Contracting Co.*, 302 U. S. 134, 58 S. Ct. 208, 114 A. L. R. 318.[9]

The Federal Home Loan Bank Act, upon which petitioner bottoms its case, was enacted July 22, 1932. This Act, of course, deals with exemption from taxation of, among other things, "advances" of Federal Home Loan Banks. The Home Owners' Loan Act was enacted June 13, 1933. Under this Act the respondents contend that the taxes herein are

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[7] Home Owners' Loan Act of 1933, c. 64, 48 Stat. 128, 12 U. S. C. 1464(a), (h).

[8] Federal Home Loan Bank Act, c. 522, 47 Stat. 725, 12 U.S.C. 1421, *et seq.*

[9] In this latter case, Mr. Justice Roberts, in the dissenting opinion said, "no one denies the competence of the Congress to waive the immunity in whole or in part"

authorized. In this connection, the Supreme Court of South Carolina made this appropriate statement:

> "It seems clear to us that if Congress did not intend to permit the taxation by the State and the lesser taxing authority to the extent and within the limits of 12 U.S.C.A. 1464(h), it would not have found it necessary to have passed such an Act when there was already in existence the Federal Statute, 12 U.S.C.A. 1433, which, under the position taken by the appellant, would prevent taxation of the notes executed by it."

The Supreme Court of South Carolina, it is respectfully submitted, correctly held that the Congress, under the provisions of 12 U. S. C. 1464(h), has permitted to the States the specific right to tax notes executed by the petitioner but to no greater extent than with respect to similar local institutions.[10]

II

Discussion of Decisions Bearing on the Question.

The petitioner contends that the decision in *Pittman v. Home Owners' Loan Corporation*, 308 U. S. 21 is analogous, is controlling and is decisive of the issues here, that being a case wherein it was held that the State of Maryland could not impose a documentary tax on a morfgage given by a borrower to the Home Owners' Loan Corporation as security for a loan made by it, the Home Owners' Loan Corporation, for the reason that the Act of Congress, under which the said corporation was created,[11] exempted from taxation the "loans" of the Corporation, and that "loans" covered the entire process of lending by the said Corporation including a mortgage given to it by the borrower as security.

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[10] R. 23.

[11] Home Owners' Loan Act of 1933, Section 4, 12 U. S. C. 1463 (c.e.f.).

The Supreme Court of South Carolina did not consider the *Pittman case* as controlling, and in addition to the reasons advanced therefor by that Court, respondents point out that the *Pittman case*, in nowise, is bottomed on 12 U. S. C. 1464(h) of the Home Owners' Loan Act, the tax provision dealing with Federal Savings and Loan Associations and providing waiver of tax exemption, as that provision was not before the Court, the loan there having been made by the Home Owners' Loan Corporation and the mortgage itself having been given by the borrower to the said Corporation as security for the loan of the Corporation to the borrower. It is apparent that the decision in the *Pittman case* does not extend itself to cover the matter here, that is to say, that promissory notes of a Federal Savings and Loan Association, with regard to which there is clearly set forth in the statute a waiver of tax exemption, executed by the association in South Carolina, to the Bank as security for an advance by the "Bank", is a tax on the "Bank", taxation of which is denied under an Act of Congress.

The question here is likewise dissimilar to that in *Federal Land Bank v. Crosland*, 261 U. S. 374, 43 S. Ct. 385, wherein the question related to a tax imposed by Alabama as a condition for the recording of a mortgage executed to the Federal Land Bank, the Federal Farm Loan Act of 1916 [12] providing that first mortgages executed to Federal Land Banks shall be deemed "instrumentalities of the United States, and as such, they and the income derived therefrom shall be exempt from Federal, State, municipal and local taxation".

The highest Courts of several States have had occasion to deal with the provisions of 12 U. S. C. 1464(h). In one of these, *State v. Minnesota Federal Savings and Loan Association*, 218 Minn. 220, 15 N. W. (2d) 568, it was held

[12] c. 245, Section 26; 39 Stat. 360, 380, 12 U.S.C. 931.

that allowing State Building and Loan Associations credit against their net taxable income for interest and dividends paid to their members was void as discriminating against Federal Savings and Loan Associations in violation of the tax uniformity provisions of the Minnesota Constitution [13] and 12 U. S. C. 1464(h) which prohibits a State from imposing higher taxes on such Federal Associations than on other similar local mutual or cooperative thrift and home financing institutions. There, the Court sets forth the purpose of the statutory exemption provided to the associations in these words:

> "The Act of Congress uses these words, 12 U.S.C.A. 1464(h): 'Other similar local mutual or cooperative thrift and home financing institutions'. The purpose was to protect federal associations from discriminatory taxation which would put them on any less favorable basis than state building and loan associations."

Here, of course, there is no discrimination in favor of State chartered building and loan associations or other similar local lending institutions.

In *First Federal Savings and Loan Association of Altadena v. Johnson*, 49 Cal. App. (2d) 465, 122 P. (2d) 84, the Supreme Court of California held that a Federal Savings and Loan Association was not exempt from State franchise taxes because it did not hold a franchise from the State, and that in view of the provisions of 12 U. S. C. 1464(h), the State may impose on a Federal Savings and Loan Association a franchise tax computed on the basis of annual net income derived from investments in both local and federal funds, where the tax is not greater than that levied on a similar State institution.

The Supreme Court of the State of Florida in a case dealing with a note executed in Florida and mailed to the

[13] Const. Minn. Art. 9, Section 1.

Columbia Bank for Cooperatives at Columbia, South Carolina, held that the note was subject to the Florida documentary tax, the same being an excise tax on the promise to pay, against the contention that the note became the property of an instrumentality of the United States before it was subject to the documentary tax and was, therefore, exempt under the Federal Constitution and the provisions of the Farm Credit Act of 1933, Section 68, 12 U. S. C. 1138. *Plymouth Citrus Growers Association v. Lee, Comptroller* (1946), 27 So. (2d) 415, 157 Fla. 893. The Court stated:

> "It is perfectly evident that if the Farm Credit Act inhibited the State from imposing the tax, it could not be done, but we have examined the terms of this act, and nowhere is it provided, in word or by fair implication, that notes executed by persons dealing with Federal banks, cooperatives, or associations shall be exempt from Federal, State, or other documentary taxes. It is hardly necessary to say that, so long as the Federal Law does not forbid such a tax, the State may exercise the privilege to impose it."

The Florida Court noted that it had examined the cases *of Federal Land Bank v. Crosland*, 261 U. S. 374, and *Pittman v. Home Owners' Loan Corporation*, 308 U. S. 21, but the Court found that these cases did not overcome the conclusion reached by the Court.

It is submitted that the reasoning of the Courts of the several States in the above reviewed cases is sound in recognizing the purpose and scope of the waiver of tax exemptions and that the same is applicable in the instant matter.

CONCLUSION

It is respectfully submitted that the judgment of the Supreme Court of South Carolina should be affirmed.

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February 2, 1961.